

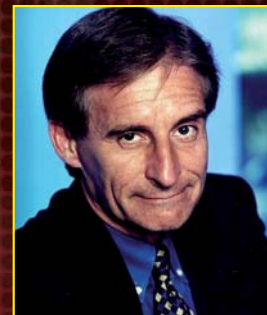
for financial advisers only

X-RAY

SPECS for advisers



January 2010



The Skandia With-Profits Analyser is designed to help financial advisers see through the opaque nature of with-profits bonds and reveal how suitable they are for your clients. **Bruce Moss** gives details.

The origin of with-profits dates back to a time before the advent of computers, to an 'era of quill pens', when actuaries balanced the interests of different generations of policyholders. Mystery was not by design – simply the result of the technology available to life offices to run with-profits.

With the passage of time, however, the mystery became part of the culture of with-profits. To some extent, life offices have used the excuse of protecting the with-profits fund as a reason to maintain the air of mystery. The theory being that investors would alter the amount they invest (or disinvest) depending on where the fund is in the smoothing cycle, ie whether the fund has distributed more or less than the asset shares backing policies.

More recently the FSA has helped to improve the situation by requiring with-profits offices to disclose more information on the workings of with-profits funds (Principles and

Practices of Fund Management), but a thorough understanding still requires considerable expertise and the investment of a lot of time.

Although the FSA has tried to improve the transparency and understanding of with-profits, it has also created an enormous problem for financial advisers as a result of its Treating Customers Fairly (TCF) requirements. Amongst other things, this requires advisers to carry out regular reviews of a customer's investments. While the FSA has issued guidance for advisers on how to undertake a with-profits review, the task is onerous and requires considerable time and expertise. Until now most advisers have been ill equipped to undertake the detailed review required at a cost which clients would be likely to pay.

help is at hand

The Skandia With-Profits Analyser lifts the veil on with-profits funds and allows advisers

to undertake a step by step review of with-profits bonds using a powerful combination of:

- with-profits analysis and data from Cazalet Consulting; and
- Towers Perrin's stochastic modelling.

This best in class combination provides advisers with the capability to deconstruct with-profits products to see how they may perform in the future. A step by step process enables advisers to review clients' existing with-profits bonds and test their suitability to meet client needs.

The question of suitability is a key one. When many investors bought with-profits policies they believed that they were investing in a fund with a high allocation to equities with some downside protection. Scientific risk profiling (ie a statistically tested psychometrical risk profile questionnaire) was not widely used and arguably it didn't need to be if you could have high equity



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exposure with the life office smoothing the returns. Because of significant changes in many with-profits funds eg a reduction in the allocation to equities, a particular with-profits product may no longer meet a client's expectations or needs. For example, the guarantee may be strong but the price may be a very low equity exposure or a high guarantee charge. The critical question is not 'is the with-profits contract any good?' – many are and have valuable guarantees – but rather 'is it suitable to meet the client's needs and expectations?'

The Skandia With-Profits Analyser takes the adviser through the review process and comprehensively addresses all the points in the FSA's guidelines.

benefits of stochastic modelling

The power of stochastic modelling is harnessed with the comprehensive analysis of with-profits bonds from Cazalet Consulting, involving:

- Assistance with the identification of the particular product and all its features.
- Data for review of the product including
 - Cazalet rating
 - details of guarantees
 - bonus rate information
 - cost of guarantees
 - potential enhancements from the life office's estate

- history of the unsmoothed returns on the underlying assets
- historic details of the asset allocation so that changes over time can be clearly seen.

- Details of the current asset allocation and equity backing ratio so that this can be assessed directly against the client's risk profile.

Cazalet data and analysis, together with details of any MVA free dates, are then used by Towers Perrin for its stochastic modelling.

The beauty of stochastic modelling is that all this information is brought to life in a way that it is easy for you and your clients to assimilate. Stochastic modelling generates a large number of plausible economic and investment scenarios and illustrates the likely returns on a with-profits product. These scenarios take all the product features into account including MVA free dates. Advisers can then clearly see the potential value of these guarantees, and if the with-profits bond is no longer suitable to meet client needs, the best time to surrender.

Stochastic modelling also allows another requirement of the FSA guidelines to be met, namely what should be done with the proceeds if the with-profits bond is surrendered. The chargeable gains calculator provided can be used to estimate the potential tax liability on surrender and the net proceeds (or any other amount) can be invested in an alternative product matching

the investor's risk profile. The option of making the switch at a forthcoming MVA free date can also be modelled. Stochastic forecasts of the range of possible outcomes (within limits – fifth to ninety-fifth percentile) are shown for the with-profits bond alongside the alternative investment.

If income is the client's objective, withdrawal payments can be set up so that valid comparisons can be made. In short the Skandia With-Profits Analyser is designed to help advisers forecast outcomes from with-profits bonds and alternative investments in like for like comparisons relevant to their clients' specific requirements.

a job well done

The Skandia With-Profits Analyser provides a state of the art tool for reviewing with-profits bonds. It sets out a process designed to meet the FSA's requirements for TCF and with-profits reviews. It transforms the complex and time-consuming task of reviewing an opaque with-profits bond from a life office which might no longer exist into a straightforward and efficient process. A comprehensive client report documents a job well done! ●

Bruce Moss is Principal at Towers Perrin.

The Skandia With-Profits Analyser is available now through the Skandia Investment Solutions adviser extranet.

www.skandia.co.uk

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